

JOINT LEGISLATIVE  
AUDIT & REVIEW  
COMMISSION

THE  
VIRGINIA  
GENERAL  
ASSEMBLY

ZERO-BASE  
BUDGETING?

Proceedings of a Forum on Legislative Oversight

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*STAFF CONSULTANT  
S. Kenneth Howard*

Zero-Base Budgeting?

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Joint Legislative Audit and Review Commission

# Preface

*Throughout the study of Sunset and related concepts of legislative oversight, the JLARC has been interested in Zero-Base budgeting. Although budget preparation is an executive responsibility in the Commonwealth, ZBB does offer an analytical style and types of information which are relevant to the General Assembly's appropriation authority. Contrasts between the strengths of the State's new program budget and strengths of ZBB forced a careful review of this innovative budget approach.*

*The first testimony on ZBB was delivered at the JLARC conference held in Roanoke in May, 1977, by Graeme Taylor, Senior Vice-President, Management Analysis Center. Taylor's testimony "Introducing Zero-Base Budgeting" was included in "Sunset, Zero-Base Budgeting, Evaluation", the first publication of the Sunset study.*

*This report is the second of that study. It is based on testimony received at a Zero-Base budgeting forum in August, 1977. Building on Taylor's outline, a panel of budget experts advised the study committee of experiences with ZBB and of its potential relevance to Virginia.*

*These proceedings were prepared using a combination of taped comments and prepared remarks. Several papers were specifically prepared for this volume. Some editing has been done by the participants and some by the JLARC staff for format and readability.*

*S. Kenneth Howard served as a staff consultant on ZBB and helped plan the organization of the forum. He prepared the introduction to this report and the first paper on budget systems. Kirk Jonas, Associate Analyst, was assigned principal responsibility for editing and producing these proceedings. He and Philip A. Leone, Chief Analyst, have shared with me in project planning, publication review, and general conduct of the study called for by HJR 178.*



Ray D. Pethtel  
Director

December 9, 1977

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# Introduction: Zero-Base Budgeting for Virginia?

S. Kenneth Howard

Change is the hallmark of state governments today. There have been extensive reapportionments, reorganizations, and constitutional revisions all over the nation. State legislatures have been caught up in this sweep too, shifting more and more to annual sessions, adding professional legislative staffs, and generally asserting more aggressively their rightful role in a separation of powers system. This publication, and the larger study of which it is a part, are just small reflections of this movement and its impact on state legislatures. In post-Watergate America, concern over legislative oversight and its proper exercise in a democracy can be found in capitols, courthouses, and city halls.

But how and on what issues should this oversight responsibility be exercised? A state legislature can look into any matter and can do so quickly or slowly, systematically or unsystematically, wisely or unwisely, and carefully or sloppily as it chooses.

## The Meaning of Oversight

Oversight as a term suggests that there is something to "look over". It implies reviews which are retrospective, looking over what has been done, in order to shape what is done or will be done. In popular terminology, such a retrospective review is an "evaluation" which entails measuring what is being done or accomplished against some criteria or standards. One issue is immediately apparent: what criteria or standards will be applied in sizing up the accomplishments? Other issues concern the techniques to be used (correlation analysis, cost-benefit studies, and the like) and the level of quantification (what measurements should be taken and how).

While these issues pose important conceptual and operating problems, the most significant concern today is less how to do an evaluation than how to get its results used after it is done. As Allen Schick pointed out in earlier testimony, in economic terms, the supply side of evaluation is strong relative to the demand side. Where is the market for completed evaluations? The cost-effectiveness of cost-effectiveness studies does not seem to be very high.

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S. Kenneth Howard has served as a special staff consultant for the Joint Legislative Audit and Review Commission for this project. An article by Dr. Howard begins on page 5.

The gap between the supply of evaluations and the demand for them provides at least part of the justification for the study of which this publication is a part. Doing "Sunset" reviews of agencies on an established timetable would generate a market for evaluations. Sunset reviews force actions, and the reviews can provide a focal point for evaluation work.

The do's and don'ts of "Sunset" itself are discussed extensively in a companion publication. Should legislation call for "Sunsetting" comprehensively throughout state government, or on a more piecemeal basis? Should agencies face termination if legislation is not reenacted, or should less drastic alternatives be provided? Over what length of time should a full cycle of reviews be required? Discussions of these and numerous other issues related to Sunset can be found in the study documents.

### Focusing on Zero-Base Budgeting

This publication has as its focus a third popular concept in the litany of modern public administration: Zero-Base budgeting. This concept has great political appeal if only because of its name. It suggests looking at government spending from the ground up, with the hope of finding ways to change that spending so other things can be done or money saved. Present spending programs constitute the largest single source of funds available for allocation by state legislatures. Can that spending be altered in some way so that other more prized things can be done? Given the growing level of government spending and the unpopularity of tax increases, it is appealing to hear that the tight fiscal situation might be alleviated by looking at existing allocations and rearranging them. President Carter's support for Zero-Base budgeting, both as Georgia's governor and as president, has given the idea political visibility and acceptability equal to its instinctive conceptual appeal.

Zero-Base budgeting's appeal is also heightened by the ease with which its procedural concepts can be grasped. It entails only three major concepts: decision units, decision packages, and rankings.

The structure of decisions units could have any one of several different foundations. A decision unit might be a program, an institution, an organizational unit, an item the legislature puts in the appropriations bill, or some other such category. To be useful, a decision unit should be recognizable, traceable over time, and deemed worthy of attention by decision makers.

Decision packages relate the resources required with the various levels of service or accomplishment that will be provided by using those resources. The nomenclature "Zero-Base" stems from the fact that the first decision package should be set at the minimum resource level needed to sustain the decision unit; if

anything less is provided, the decision unit might as well be abolished altogether. Subsequent decision packages within a decision unit build on this "Zero-Base".

Rankings are just what their name suggests: listings of decision packages in their order of importance. As a budget request works its way along, the ranking process enables decision makers at each point to choose a level of service in one area and then a level in another, before adding a second level of service in the first area. This process is obviously easier said than done.

### Three Perspectives on ZBB

The following presentations spend little time describing the mechanics of Zero-Base budgeting. Graeme Taylor's excellent paper which was presented to the JLARC study committee in Roanoke in May, 1977, and included in the conference proceedings fills this need both comprehensively and comprehensibly. There is no need to duplicate that information here.

The papers which follow build on Taylor's base of information and extract lessons from the experiences of other states as they examine how Zero-Base budgeting might be adapted to suit Virginia, given this State's existing commitment to program budgeting.

Budgeting, of whatever species, is a major administrative process in all governments and it comprises a good deal more than legislative oversight or evaluation. Revamping a major administrative process such as budgeting is arduous and hazardous work at best, especially before that system has finished its last major revamping (as is the case in Virginia). Sweeping changes should not be undertaken without a thoughtful appreciation for their implications and payoffs. The following papers may help provide some of the insights needed for such an analysis.

My introductory paper, "Budgeting as a Tool of Legislative Oversight", places Zero-Base budgeting in the context of other major budget reforms and talks about the ways in which each style of budgeting encourages evaluation work that focuses on certain criteria such as financial accountability, effectiveness, or efficiency. The paper compares what Zero-Base budgeting might provide with what the Virginia budget system does or will provide when fully implemented. It also sets forth alternative ways in which Zero-Base budgeting might be tailored to Virginia.

Although references are made in several places to experiences in other states, particular attention is paid to New Jersey where Zero-Base budgeting was introduced by the governor to counter a problem he faced in asserting gubernatorial control over his administration. Tom Bertone's presentation, "Zero-Base Budgeting in New Jersey", details this motive and emphasizes the peculiar ways



in which the budgeting process may develop when implementation takes place under such circumstances. He also suggests that under these circumstances the change has little impact on the legislature or its oversight work.

Andy Fogarty applies a Zero-Base approach to a particular Virginia institution and its programs to show how such an analysis might help the legislature improve its ability to grapple with the voluminous fiscal data it confronts during the appropriations process. His article, "How Zero-Base (Review) Could Work in Virginia", provides a concrete Virginia application of Zero-Base techniques.

Finally, Secretary of Administration and Finance Maurice Rowe outlines the basic features of Virginia's emerging program budgeting system. The paper, "Virginia's New Program Budgeting System", gives the reader an idea of how Virginia's budget system is developing.

# Budgeting as a Tool of Legislative Oversight

S. Kenneth Howard

Thus far, the commission has heard a great amount about Zero-Base budgeting as a budget system, but it has heard little about budgeting as a process. Initially, I want to give a brief overview of the budgeting process. Then I want to put into context some approaches to budgeting to show how they fit, how they evolved, what they emphasize, and where they seem to take the budget process.

Using that as background, I will then discuss ZBB in some other states, trying to extract from their experiences whatever seems most relevant to Virginia. Next, I will talk about what ZBB is supposed to provide as a system. After a brief description of what you already have in Virginia, I will suggest a variety of ZBB approaches which may demonstrate the potential usefulness or nonusefulness of the process.

## The Budget Process

Let us begin with a very quick look at the components of the budget process. There are four major steps in budgeting. The first two are the most familiar--preparation and adoption. The budget must be prepared and then adopted. The third step is equally obvious, but not as familiar because you do not work with it all the time--execution. And the last step, particularly interesting for the Joint Legislative Audit and Review Commission, is auditing (fiscal review and program evaluation).

I want to take a moment to go through each of these steps and note their location because I think that approach will highlight what can happen when you change the budget process. Preparation in Virginia, as in most of the states, is an executive

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S. Kenneth Howard is professor of political science at the University of North Carolina at Chapel Hill. He is the author of the popular text, *Changing State Budgeting*. Dr. Howard was formerly North Carolina's state budget officer. He has been elected a member of the National Academy of Public Administration. Dr. Howard received an A.B. from Northwestern University and a M.P.A. and Ph.D. from Cornell University.



function. The governor, as the chief executive of the State, provides the budget and prepares it as a starting point for legislative activities. Adoption of a budget, on the other hand, is clearly a legislative function, at least in the United States. When you say the power of the purse resides in the legislature, you are talking about the adoptive power of the legislature.

Execution, by definition, takes us back to the executive branch. The governor and the state departments and agencies execute what the legislature has adopted. That leaves auditing, which is also a legislative function. Interestingly enough, the very existence of the Joint Legislative Audit and Review Commission puts Virginia ahead of a number of states which do not properly recognize auditing as a legislative function, as an integral part of the oversight responsibilities of a legislature.

I bring this up to make the point that, when you talk about Zero-Base budgeting, you are talking about budgeting with the "i-n-g" being terribly important. Budgeting means the entire process, not something that you pick up or drop; you are talking about a process for doing all four phases. If you go to a Zero-Base budgeting system, you are talking about something that has implications for all parts of this process, not just for legislative oversight--adoption and auditing--but also for preparation and execution.

### Evolution of Budgeting

To begin a quick review of how the budgeting process has evolved, let us ask the question: "What do you expect of public agencies and programs?" I think we can list three expectations, which for simplicity's sake, I will discuss in the historical order in which they were emphasized.

First, you want agencies to be honest. It is worth noting that state and local governments preceded the national government in implementing the budget process. The federal government did not get into this until 1921. We fought and won World War I without a budget on the federal level. States and local units were well into budgeting before this. One of the reasons that the state and local levels got the jump on the federal government was the political corruption of the 1890's--probably the high point of public corruption in our history. People simply wanted to be sure that their money was handled honestly, and budgeting was seen as one way to achieve this goal. An emphasis on control was natural to assure the scoundrels did not run away with the money.

Early budget systems evolved with controls to assure honesty as a primary focus. We tend to downplay this emphasis today until there is a scandal in state government. But it remains a public desire, perhaps the most basic of all. Taxpayers insist on fundamental honesty and integrity in an operation, and when it is not present, all public officials have a problem.

Secondly, the public expects programs to be run efficiently. They want to get their money's worth. Something can be done very honestly, but also terribly inefficiently. Thus, the public wants an efficient operation as well as an honest one. In modern terminology, this concern comes under the heading of productivity, a currently popular buzz word that clearly expresses the efficiency concern.

Third, the public expects effectiveness. What are you actually accomplishing? Are you having an impact? Are the people better educated as a result of what you are doing? Is life any better? The effectiveness concern stresses program outcomes and gives a planning emphasis to budgeting.

As you would expect, budgeting systems have been devised to emphasize each of these expectations. But other devices can be used to accomplish some or all of these purposes without necessarily being tied directly to the budget process. I now want to catalog some of these budgetary and nonbudgetary approaches in terms of what they can provide.

#### Line Item Budgeting (Control)

The budget system which dealt with honesty, control, and integrity is the oldest of the group--the line item system. You are familiar with this style and have seen line item displays in your own budget documents. It is the oldest and most clearly established system of budgeting. It is one we cannot do without. No budget system has ever been devised that does not rely ultimately on line item information because you cannot run an accounting and control mechanism without line items.

There is no way to plan an activity without someone determining: What personnel are necessary? How much office space is necessary? What will travel cost? Equipment, paper, etc.? Under any budgeting process, the accounting has to go back to such line items. Somewhere in every budget process you are going to have to have line items because we have never devised a way to eliminate them. But, whether the budget is displayed by line item is a separate question.

Initially, budgets were (and still are) displayed by line item in many jurisdictions, including Virginia. But other devices can be employed to provide honesty or control. One such device is an accounting system on line items, which can be used without the budget process being tied to it. Another process is post auditing. Initially and traditionally, post audits focused on accounting to assure honesty and integrity. They say that no one has run off with the money, that all the cash is accounted for, that the assets are in place, and so forth. Auditing fundamentally and correctly stresses honesty and integrity, even today.

## Performance Budgeting (Efficiency)

The most widespread budgeting system which stresses the concerns of efficiency and productivity is performance budgeting. Interestingly enough, you sit today in the city which has probably gone further than any other with this approach. Richmond led the nation in developing performance budgets. If you have ever looked at the Richmond budget process, you have seen a highly developed and outstanding performance budget system. The Richmond budget system can tell you what it costs per fire call answered, per health inspection made, per ton of garbage collected, per mile of street cleaned, and so on. Those are essentially efficiency questions: "How much are we paying per unit of production?" Performance budget systems aim at answering such questions.

One of the weaknesses of the performance budget system was illustrated in the early 50's when New York State developed a performance budget approach for its tuberculosis hospitals. The developers came before the state legislature and presented performance budget information they had obtained. It was a very impressive display. They could tell all kinds of things about the cost of lab tests and so on in the hospitals. As they presented this to the state legislature, one wizened veteran legislator finally reared back and said, "Who gives a damn what it costs to process a pound of laundry?" He did not and that is a very important point.

For the most part, state legislators should not be concerned with what it costs to process a pound of laundry. But somebody should because that is part of the efficiency the public expects. They want somebody to be worried about whether the cost for processing a pound of laundry is reasonable or not. Whether that somebody should be a state legislator or not is debatable. We do know someone who ought to care--the person running the laundry. Such questions are clearly the concerns of program operators, whatever the program may be.

Other approaches that are used to increase productivity and efficiency include traditional organization and management devices and industrial engineering. Indeed there are a range of established professionals who promote productivity and efficiency, quite unrelated to the budget process.

A more recent efficiency development is MBO, Management by Objectives. In most cases, the stated objectives have a production connotation, the amount of production that you want to achieve is compared with the amount you actually achieved. MBO becomes a production-oriented measurement device because that is the easiest thing to measure. How many welfare cases are you going to handle? How many miles of road are you going to construct? How many students are you going to process through this program, etc.? Essentially a production objective is set and checked later to see if it has been met.

Accountants and post auditors have looked at developments in the auditing field and have said, "We do not think we should be limited". They have come up with a term called performance auditing. It is difficult to define and, depending on who you talk to, it is different things. I put it under efficiency devices because I do not like accountants doing effectiveness evaluations, but that is a personal bias--performance auditing is very much in the eye of the beholder.

For a long time, auditors and accountants who do post audits have been expected to comment on the overall efficiency with which an operation is run. When a private business wants someone to come in and see how efficient it is, a CPA is often called upon and becomes a performance auditor. He measures efficiency separate from budgeting. When performance audits are aimed at effectiveness, there is a real misnomer because the "performance" in performance budgeting has come to mean efficiency concerns, not impacts or outcomes *per se*.

#### Program Budgeting (Effectiveness)

Turning to the third expectation, effectiveness and a planning emphasis, you come upon program budgeting. The most renowned approach is the so-called PPBS (Planning, Programming and Budgeting System), a device of the early 60's which dealt with questions of effectiveness. It asks the questions: "What are we actually accomplishing? What impact are we having?"

You have heard of other devices that stress effectiveness, but they are not necessarily tied to budgeting. Evaluation is one such device which focuses on effectiveness rather than efficiency. Most of the people who have spoken to you, and most of the people who write about evaluation, are interested in effectiveness questions rather than efficiency ones. I hope the distinction between these two concepts is very clear by now.

Another type of analysis that is being talked about is Impact Analysis. What are a program's impacts? A somewhat similar device, one you are considering, is Sunset. I put Sunset in this category because most of the people who talk about Sunset talk about programs which are not accomplishing what they are supposed to. Few Sunset supporters talk about closing down programs because they are inefficient. These persons want to terminate programs because they are not doing what they were intended to do, clearly an effectiveness criterion.

#### Where ZBB and Oversight Fit

The topic of this presentation is Zero-Base budgeting, and I have not mentioned it. This is a deliberate and conspicuous omission on my part which I will now correct. Where does ZBB fit in these categories?

What ZBB emphasizes is efficiency and production, and that is where I will put it. ZBB proponents talk about the effectiveness of programs; but when you take a hard look at the process, it is fundamentally aimed at improving the management of state programs or the management of the installation where it is used. It is not fundamentally aimed at the policy making or planning process. It comes much closer to helping the laundry manager than it does the legislator, so to this extent ZBB is essentially a productivity and efficiency tool.

Finally, where does legislative oversight fit into all of this? Except for post auditing, legislative oversight activities have not been mentioned. Legislatures are like three thousand pound gorillas, they can sit anywhere they want to. Legislative oversight is whatever you want it to be. You can look at honesty questions; you can look at efficiency questions; you can look at effectiveness questions; you can do anything you jolly well please.

At any point in time, you may want to look at all three or to stress one rather than others. Nothing promotes reform or change more than a good scandal or a disaster. Depending on what caused such events, you will want to get into different kinds of questions and raise different issues. To me, legislative oversight is an umbrella term. As representatives of the public it is up to the legislature to reflect the public concern about all three expectations: honesty, efficiency, and effectiveness. All three are legitimate concerns of state legislatures. A committee or other legislative unit can appropriately inquire into any of these.

#### Relevant Experience Elsewhere

Let us now look at some of the ZBB experiences of other states to see what is most germane to Virginia. I want to start with Georgia, the granddaddy of the ZBB states. It is a story that has been heard before; and I will not go through it all, but it is one of the few states where ZBB has been in place long enough for some independent assessments to have been made of its accomplishments.

*Georgia.* One of the first things Georgia discovered was the enormous volume of paperwork involved. They started out with 10,000 decision packages but are now down to about 5,000. They also discovered that ZBB provided improved information at a number of levels of government. I should add that how much improvement can take place depends in part on how bad a system is to begin with. Nobody held Georgia up as a hallmark of good managerial information systems prior to the installation of Zero-Base budgeting. In any case, there seems not the slightest doubt that ZBB improved the quality of information available to Georgia managers. Further, ZBB clearly evoked more participation in the budgeting process throughout all organizational levels. One of the major features of ZBB is getting lower levels of management involved in the process. It clearly had this impact in Georgia.

Looking at the disadvantages, there is the paperwork which was overwhelming and still continues to be mountainous. Similarly, the ZBB process is a big time consumer. Finally and vitally, there were no discernable reallocations of state resources that resulted from the installation of Zero-Base budgeting. One basic appeal of ZBB is that it should enable decision makers to take money from one area where it is not needed on a priority basis and shift it to another. The independent reviewers who looked at the Georgia system said they could not ascribe reallocations, which did take place, to ZBB *per se*. Although that sounds like a very damaging statement, several mitigating factors should be considered.

*“ZBB can provide some things you probably want . . . you want to get into the base . . . you want to know what the alternatives are . . . you want priorities . . . and you want managerial participation. The question is—do you want to do these things by ZBB?”*

First, Georgia not only installed ZBB, but it reorganized state government at the same time. They were trying many things simultaneously, and it is very hard to apportion the impacts of those changes. The reviewers were academics and were very careful to say, "We cannot attribute certain reallocations which did take place to ZBB". If you pressed them by asking if the reallocations were therefore the result of reorganization, they would very carefully reply, "No, we do not know exactly what caused them. We do not know because both things were going on; all this was wrapped up together."

A second reason for not being able to find any significant changes is that all agency budgets were going up, thus making it very hard to ascribe to ZBB any internal shifts that may have been taking place within them. So we are unable to determine with certainty that one event caused another.

*Texas.* Departing Georgia with these very cursory remarks, let us take a look at Texas next. What I am really going to suggest is that we *not* take a look at Texas. Why not? After all, Texas is probably the second leading ZBB state and has been at it for awhile. But, Texas has never had an executive budget process. The first step in the cycle described earlier is preparation--and preparation is an executive function. Texas does not understand that idea and never has. The whole preparation process in Texas is legislatively dominated, and it does not fit Virginia's traditions, mores, or laws.



*New Mexico.* A third example which is comparable to Texas in a lot of ways comes from New Mexico. There the legislature, much as it did here, initiated or pushed for certain changes in the budget process. The reform they hit on between 1971 and 1974 was ZBB. Now, New Mexico is moving in a more programmatic direction.

Like Texas, New Mexico had a legislatively dominated budget process--the executive really did not submit much that amounted to anything. But now New Mexico is moving toward a program budget as the legislature and executive begin accommodating to budgeting in a way they have not known historically. Like Texas, New Mexico is not today where Virginia is in terms of working out legislative-executive relationships.

*Louisiana.* Less attention has been given to Louisiana where ZBB is not so highly developed. A year ago, the Louisiana legislature mandated that the state go to a Zero-Base budgeting system. And, as I understand it, they are putting about 20% of the agencies on ZBB the first year, about 50% the second year, and the remaining 30% the final year. Saving the toughest nuts for three years down the road, Louisiana did mandate the process on a phased-in basis.

It is premature to judge the impact it has had, but Louisianans do issue one warning which is significant for Virginia--do not have other major reforms going at the same time. In other words, they are saying, "If you are going to change major processes, do one process at a time. If you are going to overhaul your accounting system, your personnel system, or other things that have enormous impact on the budget, do them in a logical order. Do not try a major reorganization of state government and ZBB at the same time." Louisianans did not want to go through what Georgia went through.

A second thing Louisianans talk about is doing a lot of training. They have found that it took a tremendous amount of training time to put in a ZBB system, and they stress the need for both training and the time to do it.

*California.* California is interesting because there the ZBB approach was applied to selective programs. In other words, they select certain programs and do a ground up analysis on them. These may be pieces of a department rather than a whole department. In short, it is a selective strategy.

*Rhode Island.* Rhode Island is of interest because there ZBB is tied to an existing program budget system. Proponents in Rhode Island stress the priority ranking of various proposals which come out of ZBB and the analytic justifications. I frankly have a little trouble with the statement about analytic justifications. Analytic justification is fundamental to a program budget system, but Rhode Islanders claim that such work really got rolling only after they got into ZBB.

*Illinois.* The last state I want to mention in this group is Illinois. It is interesting from a practical operating and political point of view. They set as their base level not zero, but 90% of the existing level.

In essence, Illinois agencies were told, "You can put in anything you want up to 90% of your existing levels: old programs, new programs, anything you want. We guarantee you 90%, and you design whatever you want within that figure. But above 90%, you have to fight every step of the way. Put your proposals in priority order, justify them carefully, and be prepared to fight over them. If you think a new program is more important than something in the last 10% you already have, put it in the 90%."

Why go through all these other states? This brief listing clearly indicates there are a lot of different ways to approach ZBB. Many different styles exist, and you face many options if you want to do some portion or all of what is called Zero-Base budgeting in the states.

#### What ZBB Provides

Using material Allen Schick provided this group in Roanoke, let me highlight four things ZBB is supposed to provide. He said these results made ZBB different from other budget approaches.

First, ZBB enables you to examine below or get into the base, the bulk of government costs. I have to note, however, that you can do that in any budget system; it is only a question of how. Getting into the base is not unique with ZBB, it can be done in a number of ways, a point to which we will return later.

The second thing ZBB provides is a set of fully developed alternatives. Schick contrasts this availability with the fact that the governor makes one recommendation to a legislature. The legislature faces a recommendation, not a set of alternatives. Two caveats are in order. The first concern is the tremendous amount of paperwork involved where every program offers at least three levels of service instead of one. A whole lot of paperwork is needed to provide a wide range of choice. Also, is the legislature--particularly one which is not a full-time one--really equipped to handle the number of choices and the information flood that a list of developed alternatives entails? Or, is the legislature better off taking a reasonably well thought-out recommendation and then fighting at the margins about those particulars it does not agree with?

A third vital part of ZBB is assigning and ranking priorities among alternatives. This can also be done in other systems of budgeting, but it is one of ZBB's strong points, particularly if you go into the base.

Finally, Schick stresses participation in budgeting by managers all up and down the organizational line. Good budgeting requires some relationship between he who must manage the program and he who budgets for it. The two activities should be related but in many agencies are not. Coordination can be achieved in other budgeting systems. As a matter of fact, the earliest writings in budgeting around the turn of the century talk about involving line managers in the preparation of the budget. They should be involved no matter what budget form or system is used. ZBB may or may not be an easier way to involve line managers, but the Georgia experience suggests that it does have this important effect.

Zero-Base budgeting can provide some things you probably want in Virginia. You want to get into the base because that is where the bulk of your available resources are. You do want to know what the alternatives are. You want a sense of priorities, and you want to encourage managerial participation from different organizational levels. The question is: "Do you want to do these things by ZBB?"

#### What Virginia Has

Now let us take a brief look at what the evolving Virginia budget system already has. The new system is not completely in place, but its directions are fairly discernable. Graeme Taylor has written: "Any decision to launch ZBB should normally be proceeded by a systematic appraisal of the strengths and weaknesses of the existing budget process". In that spirit, let us look at the existing strengths and weaknesses of the Virginia budget process.

First and foremost is the program structure. You have already agreed on the categories that will be used to pull together information in the appropriations bills, the accounting system, and the budget document itself. That is no mean feat. In fact, it has taken nearly three years to get to this point, a testimony to just how hard this work is.

Secondly, the statute presently calls for three levels of effort to be displayed in the budget documents themselves: continuing the present level of service, work load increases, and new or expanded programs. If the budget document is to contain this information, everything that comes in (requests, etc.) will have to include those same categories. To this extent, you have already built in some alternatives and have concomitantly multiplied the paper flow.

Virginia's new program budget system has many strengths. The one major weakness is obvious--it does not necessarily get into the base. It provides some alternatives, but it accepts the present level as a starting point instead of digging into it. I do not believe you can make significant reallocations within your

existing resources if you accept the present level as a given, which this system does. The new system does not frontally assault the question of should you continue doing what you are.

A third characteristic of your present system is that it provides many types of measurements. Among them are measures of effectiveness, work load, and performance. Such measurements are important considerations no matter what style of budgeting you have because of the information they provide on which to base decisions.

A fourth characteristic of the present system is the attempt to specify goals and objectives. The process is trying to build into management thinking all the way up and down Virginia government the question: "What are the goals and objectives of this unit?" What you are trying to accomplish is an initial and fundamental issue no matter what budgeting system you are using. The Virginia system begins with this appropriate point.

*"Virginia's new program budget system has many strengths . . . the one major weakness is obvious—it does not necessarily get into the base . . . I do not believe you can make significant reallocations within your existing resources if you accept the present level as a given, which this system does."*

#### Question

Don't you think such matters are the function of the legislative committee that reviews and tears apart the executive budget? When they know what the present level provides, isn't it the function of the legislative committee, the House Appropriations Committee, and the Senate Finance Committee to require that the present level or base be justified?

#### Dr. Howard

Certainly it is the proper function of the committee to try to do that; but whether you have a system designed to really make people do that, except on a selective rifle-shot basis, is another matter. Committees must be selective and sporadic rather than continuous and comprehensive. There is a difference between what a part-time legislature or legislative committee can get done along these lines and designing a system which makes everybody in state government consider these issues as a regular part of the management process. Zero-Base budgeting tries to get everybody to

think in these terms. Generally, program budgets do not raise questions about the base nearly as well as ZBB, which is one reason it is so popular.

#### Question

What we are doing is a step toward Zero-Base budgeting, isn't it?

#### Dr. Howard

Well, like beauty, ZBB seems very much to be in the eye of the beholder; it depends on what you are looking for. If you are seeking a clearly organized way of challenging the base, no, the Virginia budget system is not predicated on doing that, except on a very limited basis. I think this is one of the major issues lurking in your present system.

#### Question

I think program budgeting asks about the present service or program level. You delve into it by asking what a program is going to cost and what its purpose is. You make them identify what they are doing under a projected program. We have been talking about this thing for three years now. We are trying to make them identify what they are doing, to prove what they are doing, and how much money they are going to spend in doing it.

#### Dr. Howard

I agree. That is an aim, and it is possible in a program budget system. I am trying to talk about tendencies; what tends to happen is the fact that gets downplayed. For years Virginia has operated with a line item budget system. There was no logical reason why these same questions could not have been raised under a line item system. The role of the legislature has not changed, nor has the role of the committees. The ability to raise these same questions under a line item format has always been there, and I am sure that for years Virginia legislators believed sincerely that they had some sense of what those programs were trying to accomplish. They were asking hard questions in 1920, in 1950, and in 1970 about what these agencies thought they were doing. I do not see any change in legislative concern about this matter. But a program budget system does not highlight the issue as well as ZBB does. The present Virginia system *could* be used in this fashion. But, it is more likely that a ZBB system *will* be so used. That is my major point.

#### Other Management Objectives of the Budget Process

What are some other things you need for good management in Virginia that your budget process might help you achieve?

First, you need better program planning. Sheer logic says that budgets flow from programs--programs do not flow from budgets. Expenditures should be driven by program needs, not by what comes out of the existing budget process where somebody adds 5% or 10% or does a cost calculation of some sort.

Secondly, you want more analysis. You are hoping to dig more and more analytically into impacts of one sort or another. Such activity is not well established in Virginia but it is emerging.

Third, Virginia law is well ahead of that in a number of other states because it requires that revenue and expenditure projections be prepared for a longer time period than the next budget year. You are trying to view your current fiscal situation through the perspective of a longer range six year revenue and expenditure plan. This effort is highly commendable. The projections are not all they should be yet but the pattern is clearly set.

Another process going on now, suffering very much from birthpains, political realities, and a number of other difficulties, is targeting. In my opinion, better budgeting results if, from the beginning, the people who do the budgeting and program planning know the size of the ball park in which they are supposed to play. What limit does the governor or the legislature want agencies to be thinking about rather than just drawing up Christmas wish lists? When I was budget officer in North Carolina, we let agencies blue sky every budget request. It was outlandish. We ended up with requests totaling 50% more than the current state budget. I often wished we had figured out a device for telling them the size of the fiscal ball park in which they should plan.

#### Question

Targeting has not done too well here. Although we set targets, the agencies have not adhered to them. Is that true elsewhere?

#### Dr. Howard

The reason we did not do it in North Carolina was that we could not figure out a workable way to do it. It is easy to see why you want it, but it is murderously difficult to accomplish. A lot depends on the interest of the governor and his willingness to follow through. If the agencies do not think there is a whip, and that they will be lashed for failing to observe the targets, why should they pay any attention to them? If neither the legislature nor the governor is going to use the targets or hold the agencies to them, why have them? The agencies file their requests, run them through, and leave. Targeting then has not accomplished a whole lot.

A final point on which Virginia's current system is deficient is linking operating and capital outlays. Interestingly enough, this is also a point about which Zero-Base literature never speaks. ZBB proponents almost never mention capital outlays as a part of program costs, as something that must be recognized when looking at the total costs of a program from ground zero. Establishing capital costs is not easy because most governments do not take depreciation; their records do not set it up. But capital expenses are a big part of the decisions the legislature must make. They can be political hot potatoes in a lot of ways. They can be big fiscal and operating problems.

### Alternative Approaches

Let me conclude by laying out very quickly possible approaches that might be taken in Virginia.

First, the State might adopt ZBB from top to bottom-- shift to it totally.

Second, a distinction could be made between budget review and budget preparation. The legislature could tell the governor or the executive branch to prepare the budget any way it wants to, or could enforce the existing law requiring that the budget be prepared in a certain way, and still review it differently as a legislative body. The legislature may want additional information, perhaps going so far as dual submissions. In the latter case, agencies would submit, to the legislature, not only what they submitted to the governor but additional materials separately and specifically prepared in whatever form the General Assembly might direct.

Third, selective reviews could be done. This possibility is not dissimilar from the California strategy discussed earlier. Pick out those programs you want to review and do them on a selective basis without changing the whole budget system. In essence, this is what Sunset does; it sets up a schedule which determines your selectivity. You cannot review everything in one year, but over five or six years, it might be possible. In addition, particular programs might be singled out for review at any time. Selections could be made on a completely ad hoc basis from session to session if you liked.

One device Virginia could apply would be having the Secretaries develop priorities. The priorities that go to the governor would be the ones the Secretaries assign. The Secretaries could review and prioritize all requests. A Secretary can try to do this now, but it is done sporadically. The power probably should be formalized.

Further, the State could design its present budget system to get into the base more adequately. After looking at the

problem, you may want more scrutiny of the base built into the system.

In addition, the State could press for specialized organization and methods work. In fact, a unit that specializes in organization and methods work already exists in the executive branch. You may want to beef this up. You could establish a roving team of auditors or similar professionals who would work for the legislature and be sent wherever you choose.

Finally, devices for promoting participation from all management levels can be sought. I am not talking about citizen participation or political participation but about participation by all managerial levels of state government. The system could be designed to encourage all levels of state bureaucracy to become involved in preparing the budget. Again, obtaining such participation is supposed to be one of ZBB's strengths.

### Conclusions

In sum, Virginia needs to design its own process. You need to decide what questions you want asked. Do you want to talk about impact and effectiveness or something else? Do you want to ask about efficiency? What questions do you want answered, how often, and by whom? Should a Sunset appear every five years, ten years, or two years - how often do you want this kind of issue raised? Should it be built into a legislative review process, the executive budget process or done by some other means? Should these questions be raised to everybody simultaneously as in a full ZBB system or raised selectively to particular people?

By sorting out answers to these and similar questions, a tailor-made system can be designed, selecting among a variety of options.

Once these basics have been figured out, procedures can be linked to the budgeting system in whatever seems to be the most appropriate way. Some parts may be done without any linkage to the budgeting system. Some parts would probably work better if linked to the budget system. In some cases, the choice might go either way. There are advantages and disadvantages to either approach.

### Question

When talking about participation, it seems to me you have as much likelihood of getting increased justification for the status quo as you have of making changes in the system. What incentives have other states used or what incentives could be applied at a lower level of management to encourage decreased overhead and more efficient operations?



Dr. Howard

Three responses come to mind: 1) use professional incentives; 2) use monetary incentives; and 3) it cannot be done.

What are the problems? Let us look first at monetary rewards. Any effort to reward good public management monetarily encounters questions about how much money should be provided. Because results show in profit and loss statements, businesses can measure results and do a lot of things in this regard that public agencies simply cannot.

Furthermore, the money involved is often so darned big that it becomes scary. For example, we ran a suggestion system in North Carolina and in came a very sensible suggestion that saved the State three hundred and fifty thousand dollars. How much of that are we supposed to give the individual who suggested the change--three hundred and fifty thousand dollars? That won't fly politically, even though we are going to save it every year thereafter. Obviously, there are some real problems with public monetary incentive systems.

From a policy point of view, the Illinois plan we discussed earlier intrigues me as an incentive program. You could guarantee to a program manager that he has a certain amount of money and that he can use any savings from productivity improvements as he sees fit. But, in giving him this guarantee, you lose the flexibility to shift money from his function to another.

The most positive and interesting possibilities come from professional reward arrangements. You begin by assuming that, fundamentally, people want to do a good job. Thus, if you involve such persons in ways in which they have not been involved before and enable them to do their jobs better, you are probably going to get a very positive response. They appreciate it, and they like it. Professional psychic rewards tend to be the most useful incentive in public administration. In the long run, internal motivators of this sort are probably the best. Managers seem to respond positively to the challenges of responsibility and to involvement in what is happening in their organizations. That was the biggest pay off in Georgia because they did not have monetary rewards or incentives at all.

Thank you very much.

# Zero-Base Budgeting in New Jersey

Thomas L. Bertone

When I was invited to appear, I was presented with a list of questions which I understand to be of particular interest to you. Consequently, I have structured my presentation around these questions and will attempt to answer each in turn. These questions are designed to provide you with an understanding of the New Jersey ZBB experience.

Before beginning, however, I would like to make a distinction between Zero-Base budgeting (ZBB) as a system and Zero-Base review. ZBB as a system is a set of procedures, forms, and prescriptions for preparing a budget by the executive branch of government. ZBB was not designed and has not been used primarily as a tool of legislative oversight. Zero-Base review, on the other hand, is a process for asking whether parts of a program or budget activity ought to be continued or allowed to die--questions that can be asked by officials in either the executive or legislative branches.

I come from a state with a ZBB executive budget preparation system. I will, however, be commenting on whether or not ZBB can be of value to the legislature in accomplishing the processes of budget review and legislative oversight. I will also be presenting my perspective, my interpretation, of what has happened in New Jersey. If you ask someone from the executive branch, you might get a slightly different interpretation.

## The Basis of ZBB

To begin, Zero-Base budgeting is based upon the management theories of management by objectives and management by participation. ZBB gets managers involved in preparing the budget

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Thomas L. Bertone is Acting Executive Director, Office of Fiscal Affairs, New Jersey State Legislature. Dr. Bertone's professional experience includes duties as a budget examiner with U. S. Bureau of the Budget, as a management analyst for the 8th U. S. Army Comptroller in Korea, and as a private management consultant. Dr. Bertone received his bachelor's degree in government from Harvard University. He received a M.A. in political science from Stanford and a Ph.D. in public administration from George Washington University.



and shifts the fundamental decisions on the budget from the central budget office to line managers who submit the budget through the system and themselves provide the major budgetary alternatives to the chief executive.

In addition, there are the familiar components of ZBB. These include decision packages related to outputs and organization objectives, priority rankings of decision packages, Zero-Base review, and alternatives for incremental decisions at the margin. These items have been explained by previous speakers, and I shall not redefine them here. Suffice it to say that all of the items are, at least in theory, present in the New Jersey ZBB system.

Operationally, ZBB is accomplished by giving a set of forms to a manager and requesting him to complete them. That is the method by which he is led to address the questions: "Shall we kill the program? What are your priorities?, etc." In filling out the forms, he answers these questions. Thus, in ZBB, as in most budgeting systems, the primary operational element involves giving someone a set of forms and requesting their completion. Beyond this, the system is qualitatively dependent on how well these forms are completed.

#### Why ZBB was Adopted in New Jersey

The actual decision to implement ZBB, however, can be complex. In addition to the theoretical, professional reasons for adopting ZBB, there may be practical, political motivations as well. In my opinion, these motivations manifested themselves in the decision to implement ZBB in New Jersey.

Zero-Base budgeting was adopted in New Jersey for three reasons: (1) to give a newly elected administration a political initiative; (2) to break the power of the central budget director; and (3) if it could also be accomplished, to improve budgeting in the State of New Jersey.

I expect that most of the presentations that you have heard present ZBB as if it were a tool of professional budgeteers to improve budgeting. What you find in New Jersey, at least, is that the real reason for implementing ZBB was political and that budgeting is, in fact, a political process. It is important to realize that, when you start dealing with who makes decisions on budgets, you are involved in a political process.

Let me give you some background on these comments. Brendan T. Byrne took office as the new Governor of New Jersey in January, 1974. He was interested in developing some kind of new program, a new series of initiatives. He brought with him Dick Leone. Dick Leone had been his campaign manager, held a Ph.D. from Princeton, and was teaching at Princeton prior to joining the Byrne campaign.

Leone was aware of what was happening in public administration throughout the country, familiar with the literature; and he brought that background with him when he was appointed treasurer for New Jersey. The Department of the Treasury in New Jersey is the department where all financial activities are centered--investments, accounting, budgeting; the entire financial operation for the executive branch is located in that one department.

The new Governor and State Treasurer came in, and they looked at the budget system, and they didn't see a budget system--they saw a personality. That personality had been in the budget bureau for 30 years and was a very strong personality. He was Mr. Budgeting in New Jersey. He controlled the system. He controlled, in essence, the information that flowed to the State Treasurer and to the Governor for making decisions on the budget.

In 1973, Governor Cahill's last year, the budget had been presented to the Governor with a surplus estimated at \$27 million. When that estimate was presented to the legislature, the legislative Office of Fiscal Affairs responded that the estimate

*“ZBB was not designed and has not been used primarily as a tool of legislative oversight. Zero-Base review on the other hand . . . (involves) questions that can be asked by officials in either the executive or legislative branches.”*

was grossly understated and that the surplus was going to be substantially greater. By the summer, it was obvious that this was true; and the surplus eventually turned out to be in excess of \$300 million. This had severe political impact in the midst of the gubernatorial campaign.

Brendan Byrne came into office, and the estimate was presented on revenues for the new budget. This time the Office of Fiscal Affairs argued that the estimate was overstated. By the summer, it was clear that this was to be the case and that there was going to be a budgetary crisis with revenues falling below the estimate.

Thus, the Governor and State Treasurer were facing a budget that did not give them information they could rely on. There was the question of what to do.

Although a program budget was technically in place, analysis was being done on the basis of line items instead of programs. The budget director relied heavily upon his judgment and his experience in budgeting. There was dissatisfaction with this situation to the extent that at least one important subordinate wrote a letter to the new administration suggesting that there should be improvements in the operation of the budgeting system.

#### A Desire For Initiatives

Thus, we find a new administration wanting a political program, some new initiatives, realizing that they were basically at the mercy of a central budget director in terms of budgets, and realizing that there were improvements that could be made to the budgeting system. We also had a State Treasurer who was aware of what was going on in public administration and aware that Jimmy Carter had instituted ZBB in Georgia.

The administration could not advocate program budgeting because program budgeting had already been implemented, and they could not play that message publicly again. So they went to the obvious solution, a Zero-Base budget. In my opinion, Zero-Base budgeting was initiated in New Jersey as a result of this complex political environment.

If you are faced with that kind of situation--if you are a new administration and you want to grab control of the budget from a central budget office--then a ZBB system makes good sense. You can pass out a series of forms and say "fill them out", and, if the system works as it is supposed to, the alternatives come up from the line managers. With this system, the central budget office can be bypassed to some degree.

I am not sure that the new administration understood the power of ZBB for this purpose. But it was there on the shelf to be used, and they used it. That was the reason for implementing ZBB in New Jersey.

#### The Transition From Line Item to ZBB

The major transitional problem from the old budget system to the new system has been loss of interest. There was some resistance to implementing ZBB by the central budget director, as you might imagine. Apparently, he argued that ZBB could not be implemented the first year, that it had to be delayed until the second year. I assume that when the administration got to the second year, he would have argued that some problem prevented implementation that year. Nevertheless, the Governor insisted that ZBB be implemented the first year. Be that as it may, the central budget officer chose to retire in September of 1974; and

with his retirement from the scene, the rationale for continuing with full ZBB implementation also disappeared.\*

By then, however, the forms had been distributed, the agencies had completed them, and the Governor could go before the public and say, "We have introduced ZBB into our budgeting system."

This brings us to the professional, technical problems of implementation. The first problem has been one of coverage. We have expenditures in New Jersey of about \$7 billion and an appropriated budget of about \$4 billion. Of that, the ZBB system extends to only \$300-\$400 million. The higher education people, for example, argue that they have a formula budget; the human services people argue that they cannot do ZBB on welfare and medicaid. In short, to the extent that we ZBB at all, we ZBB on only about eight percent of our budget.

The second problem is that the quality of information that we get is poorer than the quality of information we get in the program budget system--and there is less of it. I would guess that the quality is poorer in ZBB than it is in the program budget primarily because the Governor does not use the ZBB information for his decisions. Since the Governor does not use it, the departments do not pay much attention to quality in completing the forms.

Let us now examine the contribution that ZBB has made to the executive branch. In general, the contribution of ZBB, aside from its political benefits, has probably been very little--particularly in terms of improving professional budgeting in New Jersey.

In judging the contribution of ZBB, however, let us look first at the process. In theory, the line manager is supposed to rank his programs, make decisions on the budget at his level, and pass it up for marginal decisions, incremental additions or subtractions, at the next level. There is no indication, no evidence, that this happens in New Jersey. The process seems to be as it was before. The forms are completed. They are sent to the central budget office. The central budget office simply uses them as an information increment in its preparation of recommendations for the chief executive. The departments, the managers, continue to use the program budget forms to ask for as much as they think they can

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\*These comments are not meant to reflect in any way upon the professionalism of the budget director. Problems with revenue estimates may have been reflective of the quality of information available at the time; problems with ZBB discussed below may suggest that the budget director was correct about implementing ZBB; and most budgeteers know that it is very difficult to obtain good and helpful analyses and appreciate the value of experience and judgment. Rather, these comments are meant to suggest only the role that power relationships, desire to control events, and access to information may have played in the decision to implement ZBB.

get, and those requests, sometimes two and a half times their prior budget, are made to the central budget office. The central budget office reduces the departmental requests and presents recommendations to the Governor for decision. The decision process has not really changed.

#### The Results of ZBB--Outcomes

Secondly, let us look at ZBB outcomes. There is no evidence that the decisions on the budget now are any different than they were before. We had a severe budgetary crisis in New Jersey that lasted for two years. The first year the Governor submitted a budget that he intended to balance with a half billion dollar income tax program. The second year he submitted a budget which was balanced, and he maintained that he had to cut requests two to three hundred million dollars below the prior year appropriation in order to do that. But the cuts were political decisions, not Zero-Base budgeting decisions.

The political decisions were made in the following manner. We have a General State Operations portion of the budget, a State Aid portion of the budget, and a Capital Construction portion of the budget. Capital construction projects were simply deferred until better years. General State Operations went up roughly to equal cost-of-living increases. The cuts were made in State Aid. The Governor merely cut out grant programs, anticipating that local governments would then press the legislature to restore these programs; and the State would get an income tax. There is no evidence that ZBB affected that political decision or budget cutting process.

There were also some programs in General State Operations that were addressed, but these programs were addressed on the basis of information and analysis that preceded ZBB. Meat inspection was killed because we knew the Federal government would pick it up. That idea had been around for probably five years. The vehicle inspection program was suggested for elimination, but that was based upon a series of analyses that preceded ZBB, analyses done primarily by the legislature. The agricultural college was also identified for some reductions; but, again, that had nothing to do with ZBB.

So, in terms of what we in the Office of Fiscal Affairs perceive to be the decision-making process, there has been no change. In terms of the output, the results of the decisions, we see no relationship between ZBB and the decisions that were made.

#### Limited Legislative Use of ZBB

Having seen how the executive does not use ZBB, we should ask, "Does the legislature use ZBB as a tool of legislative oversight in New Jersey?" And the answer is, "Almost not at all."

First of all, ZBB was implemented by executive decision with literally no legislative participation. I expect that a majority of the Joint Appropriations Committee now knows that we have a ZBB operation in the executive, but that is about the extent of legislative involvement. We in the legislative budget office receive the program budget request forms along with the ZBB forms. We do not provide either set of forms to the legislators themselves because the process of analyzing them is a responsibility that has been delegated to us.

The question is, "Does ZBB help the legislative budget office in doing its analysis?" The answer is "no" for two reasons. First, the purpose of legislative budget review is to address the recommendations of the Governor, to know what the Governor recommended and why he did it and what his alternatives were. That is what we try to key on.

*"Improving budgeting in a professional sense is a time-consuming process that occurs over a period of years, and it ought to be treated that way. Once you have started down the road to a program budget, you probably ought not intercede and introduce ZBB. You ought to concentrate on perfecting the program budget."*

Our budget continues to be presented in a program budget format. We look at that and try to identify why the Governor made his decision, what was the basis for his recommendation, whether it was solidly based on fact or not, and what were his alternatives. I think that if we keyed on ZBB, which is something he does not use, we would be wasting our time. If he was using it, then we would probably focus on it. If it was a complete system and this was the way budgetary decisions in the executive branch were made, then it would give us a starting point. This takes us to the second reason and the question of information.

The information that ZBB provides in New Jersey is summary information, and the quality is poor. It is not sufficient for making a decision. All we can do, in the best situation, is identify what the decision is and use that as a basis for doing our own in-depth analysis. ZBB forms and the ZBB process do not really help other than perhaps to give us a starting point. (This is essentially true also for the program budget information.)

There is one item of information that we occasionally use from ZBB forms. The forms identify, to the extent that you believe them, the subordinate manager's priorities. Consequently, we



occasionally identify an item for reduction or elimination; and we say, "This was low on the priority ranking of the department head." The legislature has never found that argument terribly persuasive, however, because the Governor apparently assigned a different priority to the item; and his is the one that counts. There is some possibility that drawing a distinction between what the department head thinks important and what the Governor thinks important is useful. Here, however, one is considering whether departments ought to be run by the chief executive as President Nixon believed, or by department heads and subordinate managers as President Carter seems to believe. I do not know the extent to which a legislature wants to get involved in that kind of issue.

Since I have given this rather gloomy picture of the value of ZBB for legislative oversight, let me now make several other brief points that respond directly to your questions.

ZBB has required no restructuring of the legislative budget review process or of the committee system. ZBB has resulted in no direct benefits to the New Jersey legislature. In sum, ZBB has not been terribly helpful to the legislature in New Jersey. Now you may find this dissatisfying. I must remind you, however, that New Jersey started out to implement ZBB, lost interest and, therefore, does not have a complete ZBB system. We really have the program budget system as we had it before with some supplementary information provided by ZBB. (There are now indications that our executive branch has a renewed interest in ZBB and may attempt a complete implementation of ZBB.)

You could ask me whether ZBB would be helpful to the legislature if the system were fully implemented. Let me make a series of comments in that regard. In these comments, I will discuss some of the issues addressed by the previous speaker. I think that you will find what I am saying very consistent with what Dr. Howard said.

#### Compatibility With Program Budgeting

The questions that are asked by ZBB are compatible with a program budget system. Furthermore, I think that an emphasis on questions of program effectiveness is appropriate--in my opinion, effectiveness questions are more important than efficiency questions. I agree with Dr. Howard that ZBB focuses on efficiency and program budgeting on effectiveness. Thus, if you decide to improve your budget system, I would suggest perfecting the program budget system that you have. The real problem is in developing a good program structure, getting good information, and doing good analyses. That takes time.

Improving budgeting in a professional sense is a time-consuming process that occurs over a period of years, and it ought to be treated that way. Once you have started down the road to a

program budget, you probably ought not to intercede and introduce ZBB. You ought to concentrate on perfecting the program budget. At some point in the future you can address the question of greater participation by managers. I think I would argue that the program budget system gives you as much participation as you need, but that is a different question. From my viewpoint, it makes sense for you to perfect the system you already have.

### Legislative/Executive Relationships

As far as legislative improvements are concerned, I would point out the difference between budget preparation and budget review. It makes very little sense for a legislature to try to force a detailed budget preparation system on a chief executive. If it is true that the chief executive has responsibility for preparing the budget, then he probably ought to be allowed to choose the system for preparing that budget. Furthermore, if he does not use your system, you are going to have a situation in which the department heads are not responsive to your concerns--they are not going to give you good information, and they are not going to give you information that will embarrass the Governor. Consequently, it probably ought to be left to the chief executive to develop his own budget preparation system.

Now I think that the legislature can certainly identify the format of the budget that it wants presented to itself, and it can identify any separate items of information that it wants submitted. The legislature can take certain actions on the appropriations bill to require this information. It can work over a period of years to try to perfect the flow of information.

In addition to the format that you specify for the presentation of the budget, you can develop a good analytical staff in the legislature; and you can support that staff in its requests for ad hoc information. Legislatures normally specify a very few items of information for routine submissions. The legislative staff has numerous additional ad hoc requests that are necessary for budget analysis. These requests probably will not be well received by the executive. They need legislative support.

My next comment emphasizes the difference between budget review and budget preparation. The Governor has the responsibility for budget preparation, not the legislature. Agency requests nearly always exceed, by huge amounts, the resources available. Departments represent services and, consequently, develop a constituency. Someone has to make the decisions which balance expenditures and resources, and the Governor does that. He sends the legislature a balanced budget.

The political question in every state legislature I have seen is, "What is the value to the legislature of cutting things out of that budget to make allocations?" Every time you cut

something out, you make some constituency angry; and I am not sure you get equal benefits back from where you place that money.

So the Governor does a very useful thing, in a political context, by balancing the budget. Few legislators are in a position to go into the budget and make the kind of wholesale changes that the Governor must make--both because of time constraints and the political problems of changing budget allocations. The job of the legislature is one of review, to assure that the Governor has performed well in preparing his budget.

There are many things involved in preparing a budget, and Dr. Howard identified them very well. There is the problem of control. There is the problem of efficiency. There is the problem of effectiveness. There is the problem of resource allocation. All of these problems have been looked at and addressed before the budget comes to you.

The question to the legislature is, "How well did the Governor prepare the budget?" Or, "How good is the budget?" I think that the legislature should not tie itself to one approach in evaluating the Governor's performance. You should not ask only Zero-Base questions. You should not ask only effectiveness questions, or only efficiency questions, or only resource allocation questions. You should have the ability to ask all of those questions at any one point in time. And you do that, in my opinion, by developing a good staff and telling them, "Go out and find in this budget what you believe to be the most important things that should be brought to our attention this year."

The staff then reviews the budget, develops in-depth analyses for individual items, and presents these analyses for your consideration. In that way, the legislature reviews the many functions that are incorporated in a single budget document. Flexibility, I think, is the key to legislative review.

### Sunset and ZBB

Zero-Base review and the Sunset process are related. It seems to me that the current interest in Zero-Base review and Sunset is politically generated. It does not really reflect professional budgeting interests. This political interest is a reflection of a belief held in legislatures and electorates throughout the country. Among legislators and the public there is the belief that somehow government is doing a whole series of things that it should not be doing and that, if we really look at those things and asked hard questions, we can cut them out. So the issue is, "Is that true?"

If this is a correct definition of the problem, then the issue is a public issue and should be resolved by a process whereby the public, the citizens, can focus on the process and see what is

happening. We must either verify or reject the proposition that government is doing a lot of things that it should not be doing. Consequently, a separate process, a Sunset process, makes some sense.

Furthermore, if you are committed to a comprehensive Zero-Base review and to verifying or rejecting the proposition that the government is doing a lot of things that it should not be doing, the legislative appropriations process does not lend itself well to such an undertaking. The process may be able to accommodate an effort to eliminate a specific program here and there. But experienced appropriation committee members know that a proposal to eliminate a program will bring forth heated political opposition and that it is very difficult to eliminate a program in the appropriations act. The most that can be hoped for practically is to raise the issue so that it can be pursued in the following year or two, during which time additional analysis can be made and the public support that is required for elimination can be marshalled. Any effort to eliminate multiple programs will almost certainly stall the entire appropriations process and defeat the purpose of the process--which is to produce a budget. Consequently, Zero-Base review in any widespread sense is really not a process for the appropriations committee.

Neither do I believe that comprehensive Zero-Base review is suitable for your program evaluation operation. Program evaluation does address program terminations. Program evaluation also deals with more complicated, complex questions and does not simply stop at whether we should kill or continue. Your program evaluation organization probably ought to be allowed to continue in the mode in which it is currently operating.

More specifically, Tennessee's Sunset law offers three alternatives: (1) eliminate the program; (2) continue the program; or (3) modify it. Now I suspect that most of the work done in your program evaluation organization focuses on modification. On the other hand, I expect that a Sunset process is going to focus on eliminating or continuing. If the decision is to eliminate, there are no problems. On the other hand, if the decision is to continue, then the legislature has to gear up its machinery to reinstate the program and probably cannot take the time to worry about modification (or the additional time required for the evaluation to include modification). After the program has been reinstated, attention can be turned to modification.

So it would appear that the comprehensive Zero-Base review is not best suited to the legislative appropriation process or to program evaluation. It is best suited to a separate process that has clear press focus, and clear legislative focus, and has results which will be apparent to all. I admit that, if necessary, the appropriations committee can attempt it; and I admit that, if necessary, the program evaluation organization can do it. My best judgment is for a separate process.

### ZBB Not A Legislative Tool

In conclusion, then, ZBB as a system is not a legislative tool. It is an executive tool for preparing the budget. In my opinion, there are better tools. The more important questions in budget preparation are resource allocation questions and effectiveness questions. Therefore, if you are seeking improvement, you ought to focus on systems which emphasize these questions, and that means program budgeting. Think about other questions at some future date. Program budgeting will accommodate them. Furthermore, you need to work with whatever system the executive is using to make his decisions, because you are responding to those decisions. The key is flexibility in the appropriations review process, and for that you need a capable staff that has the ability to ask any questions that seem relevant in any year. That staff needs your support in getting information out of the executive. A possible means toward this end lies in specifying the budget submission format. Finally, the Zero-Base review of programs is a worthwhile exercise but is primarily a political, public problem that requires high visibility. A separate Sunset process, independent of the legislative appropriation process and of program evaluation seems advisable. With that, I will be quite happy to answer any questions you may have.

### Question

Do you know of any other states which have had an experience similar to yours in New Jersey?

### Dr. Bertone

New Mexico and Montana attempted a Zero-Base budgeting system for the legislature and rejected it. (I now understand that New Mexico has a second Zero-Base exercise in process.) The problem with this statement is that the principle staff to the New Mexico legislature on budget review moved on to Montana. So, when I say New Mexico and then Montana are two states that had experience and rejected it, I do not know whether the influence of one or two personalities led to the conclusion to reject ZBB or whether the conclusion is based on widespread dissatisfaction.

### Question

You talked about the philosophy of the appropriations process, what the appropriations committee ought to do. What you suggest is to look at the executive budget and to target various areas that we have a particular interest in, not to try to analyze every single expenditure in the executive budget, and then do a Sunset process. You seem to be suggesting that a thorough analysis of the various departments and agencies be made regularly but only every six or seven years.

Dr. Bertone

I think that there should be two separate processes. I think the staff to the appropriations committee should review the entire budget. But they should be selective in what they then present to the Appropriations Committee. The budget will get a total review, but by the staff rather than by the committee. The committee should spend its time on priority items.

In terms of the Sunset process, I would agree with what you just said, if there is some kind of mechanism for setting priorities. A Sunset evaluation is going to be time consuming and expensive and difficult, and I think that it is probably only worth devoting those kinds of resources to programs that have problems. Therefore, if I were doing it, I would opt for establishing some kind of mechanism for deciding which programs are going to get it, which ones are worth it, and which ones are not. And maybe for public argument, every program should get a review sometime.

Question

We have some of our major problems, and I think those of other states have been, in revenue estimates. In other words, in Virginia, since 1972 we have overestimated our revenues so we have had the problem of cutting appropriations on a crash-type basis. In New Jersey, how much does the General Assembly get into revenue estimates? Does the executive direct revenue estimates and follow them personally or does the legislature?

Dr. Bertone

The Office of Fiscal Affairs was established about five years ago, and with that came a revenue estimating capability.

Question

Capability for whom?

Dr. Bertone

For the legislature. Every year, the Governor presents his budget early in February. We begin doing our own revenue estimates in January. We present our own revenue estimates, and we do it in terms of a range and a point estimate. That is, we give a minimum estimate, a maximum estimate, and a point estimate, which we consider to be the most realistic estimate of revenue. Then we compare the Governor's estimates to our range. If the Governor's estimate falls within our range, we make a statement to the legislature that the Governor's estimates are realistic; he has done a responsible job. Normally, and it would be very unlikely that his estimate would fall precisely on our point estimate, we make a supplementary statement that, though he's done a responsible job, we think that a better estimate is the one we have produced.

Question

Do you reduce the budget to that estimate, or increase the budget to that estimate?

Dr. Bertone

Two comments. In the first three years, the Governor's estimate fell outside the range. Since then, they have been falling within the range. We have a revenue subcommittee of the Appropriations Committee that meets, hears testimony from our analysts, and testimony from the executive. Then it develops its own revenue estimates which tend to fall between the other two.

Question

Yes, but do you adjust the budget? In other words, if the Governor's budget is based on his revenue estimates, do you adjust it to conform to your revenue estimates?

Dr. Bertone

What we have discovered, and I suppose I could get a new lesson next year, is that the legislature or the committee is pretty good at deciding how to allocate resources if we can make the resources available. Now I just made a presentation that said there is not much to be gained by a legislature in making wholesale reductions in appropriations. However, if we can show selected reductions that make good sense, the committee will take those reductions, as well as increased revenue estimates, and focus on reallocating those resources for increased appropriations. The answer is "yes". The committee makes appropriation decisions that are consistent with its revenue decisions.

Question

How do you get funds for capital outlays?

Dr. Bertone

We have two methods. We have current revenues and bond funds. About a year ago, we passed a law capping the state budget. The state budget for general state operations and current revenue capital construction can increase only at a rate equal to the growth in per capita income in the state. Consequently, there is now a problem of being able to squeeze large capital construction projects into the budget, and we are pretty well stuck with the level of capital construction that existed in the base year. If we suddenly had a need for a \$50 million project in one year, we would have to go to bond funding.

Question

But next year, the legislature can change that cap, can't they?

Dr. Bertone

Yes, and I expect that will happen someday.



# How Zero-Base (Review) Could Work in Virginia

Andrew B. Fogarty

Thank you Mr. Chairman, members of the commission. When Ray asked me to put this presentation together, he emphasized the need to discuss the weaknesses, as well as the strengths, of Zero-Base budgeting (ZBB). After hearing Tom's presentation, we surely do not have to worry about the problems of ZBB being ignored by this panel.

Rather than dwell on the very important issues raised by both Tom and Ken Howard, however, I would like to move now to a brief discussion of how some components of ZBB could be applied to an existing program area within Virginia state government. Please keep in mind that while the programs, institutions, and current funding levels I will use are real, the example itself is hypothetical and solely of my creation. It is based on my assumptions of what may happen in terms of resource levels. But the client data are correct and the current expenditure levels are correct.

## The Language of ZBB

To establish a point of departure, let me quickly review basic ZBB nomenclature (Table 1).

Table 1

### BASIC ELEMENTS OF ZBB

- identification of "decision units"
- formulation of "decision packages"
- priority ranking of "decision packages"

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Andrew B. Fogarty is the Director of the staff of the House Appropriations Committee. Mr. Fogarty was formerly a Senior Fiscal Analyst for the Florida House Appropriations Committee and a Management Systems Analyst for the Atomic Energy Commission. Mr. Fogarty is a candidate for a doctoral degree at Florida State University. He received his M.P.A. from the Graduate School of Public Affairs of the State University of New York.



The first element displayed is that of a "decision unit", by which we mean the lowest level of program responsibility for which a budget entity is created. The scope and resource levels encompassed by decision units can vary greatly within a ZBB system, but, as a rule of thumb, they should reflect the structure of actual management decision within a program and be of sufficient importance to merit continued management scrutiny.

A continuing dilemma inherent in the selection of decision units is the problem of their number. Too many units will inevitably overload top management's ability to review each separately; too few will aggregate cost and client data at a level too general for good analysis.

The second element displayed is that of a "decision package", by which we mean explicit sets of services or activities--each of which has a price tag attached to it. A manager ranks packages in order of his or her priority, with the first package normally containing a "survival" level of resources below which the unit could not exist. Additional packages display higher levels of services, with concomitantly higher levels of costs.

Third, the priority ranking of individual decision packages represents the final step within an agency's ZBB process. At this point, top management has the very difficult task of deciding what priority to assign to each decision package submitted by each decision unit.

#### Potential Benefits of ZBB

Having gone through this demanding and, at times, conflict ridden process, what potential benefits can we look for a ZBB system to provide?

As indicated on Table 2, and despite real operational problems that should not be understated, I believe ZBB can be of value to State government particularly if applied selectively and with adequate preparation beforehand.

Table 2

#### POTENTIAL STRENGTHS OF ZBB

- complements a program budget structure
- allows "informed" decremental budgeting
- involves program managers in budget process
- explicitly identifies program outputs with program costs
- explicitly identifies program priorities

A singularly important strength of ZBB in those states using a PPB system is the fact that it helps to "fill the gaps" of a program structure, and thus complements the budget process already in place. Since Virginia hopes to utilize a program budget system for the upcoming biennium, ZBB does offer a tool whereby program data can be viewed in terms of the ZBB elements we have discussed--without the necessity to alter our newly created program structure.

Secondly, in those budget sessions marked by pronounced resource constraints, ZBB allows decremental budgeting to be accomplished on something other than an across-the-board method of reduction. Though "survival level" decision packages are the bane of any program manager's existence, they have the potential to be used as a trade-off for higher priority efforts within the same agency, if cuts are unavoidable.

Third, since ZBB dwells upon decision unit data, it tends to involve middle management personnel to a greater degree than, say, a pure PPB system. Proponents of ZBB, particularly President Carter, believe that this involvement is essential for making programs more efficient and effective at the service delivery level.

The final two benefits of ZBB must be viewed with more hope than substance at the present time. Quantification of program outputs, as well as methods of measuring interprogram utility, are clearly beyond the current capabilities of most governmental efforts. We are no exception in Virginia, but should real progress be made in these areas, a ZBB approach offers a vehicle for ready application of such data to budgetary decision making.

#### Inherent Administrative Limitations

Budget reform movements in this country have generally been advocated without sufficient appreciation of the limits of actual administrative and program capabilities of our governmental programs. ZBB, in my judgment, is no exception to this characteristic, and this circumstance reveals some potential weaknesses of ZBB (Table 3).

Table 3

#### POTENTIAL WEAKNESSES OF ZBB

- presupposes existence of adequate and timely accounting, personnel, and property management data

- for comprehensive application, requires massive amounts of resources
- requires clear program goals and objectives

First, for the system to be timely, accurate and useful, the managers preparing and reviewing budget requests must have cost and program data that fulfill these requirements. At a minimum, this requires well functioning accounting, personnel, and property management systems that can serve both intra- and interagency purposes. Once again, Virginia and other states do not currently have such systems upon which to develop a comprehensive ZBB system.

Second, from those states that have tried to implement ZBB across the board, we have learned that such an exercise involves massive amounts of paper, staff time, and management review. Thus, it is by no stretch of the imagination a "costless" process - costs are very real and unavoidable at all levels of budgetary decision making. The more comprehensive the application, the more serious the drain on decision-making resources.

Finally, and on a more theoretical plane, without clear and quantifiable program goals or objectives a ZBB system, as is true of any budget reform based on economic rationality, cannot function as its proponents would advocate. Instead of dealing with obvious paths of effective resource allocation we must, at present, be satisfied with suboptimal strategies that make the best of insufficient or highly tentative causal data.

#### Applying ZBB to Virginia

Now we are ready, perhaps more than ready, for the subject at hand--ZBB applied to Virginia. As you can see from Table 4, I have selected the Institution Services subprogram of the State Mental Retardation Services program.

Table 4

#### COMMONWEALTH OF VIRGINIA MENTAL RETARDATION SERVICES PROGRAM STRUCTURE

Function	Individual and Family Services
Subfunction	Detection, Diagnosis, and Treatment
Program	Mental Retardation Services
Subprogram(s)	Community Services, Cooperative Services, *Institution Services

To be more specific, we will focus on a single institution within the five that now comprise this subprogram, the Northern Virginia Training Center for the Mentally Retarded in Fairfax, Virginia (see Table 5).

Table 5

SUBPROGRAM: INSTITUTION SERVICES

Budget Entities: (5)

- Lynchburg Training School and Hospital
- Northern Virginia Training Center for the Mentally Retarded
- Southeastern Virginia Training Center for the Mentally Retarded
- Southside Virginia Training Center for the Mentally Retarded
- Southwestern Virginia Training Center for the Mentally Retarded

To provide a general overview of some of the salient characteristics of the institutions that now provide services to our mentally retarded clients, I have arrayed on Table 6 five measures that usually receive scrutiny in the budgetary process.

As you can see, our systemwide average daily census (A.D.C.) is slightly below total rated bed capacity, but this is not the case in each of our institutions. A current policy goal of the Governor and the General Assembly is to reduce the census in our older centers - Lynchburg and Southside, and to raise it in our newer centers - Northern Virginia, Southeastern Virginia, and Southwestern Virginia. Though treatment in the newer institutions is costlier than in the old, they are able to provide higher levels of services that will hopefully allow our retarded clients a shorter institutional stay.

Question

I understood you to say that the program budgeting that we are underway on will not give us the information that you have just referred to now. But, we can get that information from the program budget?

Mr. Fogarty

Yes sir, we have it, there is no doubt about it. We can get it if we ask for it.

Question

That is not unique in a Zero-Base budget?

Table 6

## MENTAL RETARDATION INSTITUTIONS

	FY 1977-78 Expendi- tures (Millions)	Total Staff	FY 1977-78 Cost Per Day	FY 1977-78 Average Daily Census	Rated Bed Capacity	A. D. C. + (-) Capacity
Lynchburg Training School and Hospital	\$22.2	2,325	\$35.50	2,289	2,259	30
Northern Virginia Train- ing Center for the Mentally Retarded	4.2	319	68.90	222	285	(63)
Southeastern Virginia Train- ing Center for the Mentally Retarded	4.9	360	93.50	162	200	(38)
Southside Virginia Train- ing Center for the Mentally Retarded	10.0	1,182	28.50	1,024	964	60
Southwestern Virginia Train- ing Center for the Mentally Retarded	<u>4.5</u>	<u>345</u>	<u>76.80</u>	<u>165</u>	<u>226</u>	<u>(61)</u>
Totals	\$45.8	4,531	\$39.80	3,362	3,934	(72)

Mr. Fogarty

It is not unique in a Zero-Base budget, true. I was just reemphasizing what Dr. Howard said. There is no other system of budgeting that requires the decremental/incremental approach in terms of service level, as ZBB does. And maybe Table 7 might be a little bit more helpful in explaining that.

If we view institutional services from a systemwide FY 77-78 perspective, we see that the four decision packages arrayed on Table 7 reflect increasing levels of services that can be provided during FY 78-79 at increasing levels of cost. If the State

Table 7

## SUBPROGRAM: INSTITUTION SERVICES

<u>Decision Packages</u>	<u>FY 1978-79 Cost (Millions)</u>	<u>Cumulative FY 1978-79 Cost (Millions)</u>	<u>Percentage FY 1977-78 Expenditures</u>
(1) Minimum Services, 3862 Clients	41.2		90%
(2) Current Services, 3862 Clients	7.3	48.5	106%
(3) Current Services, 3934 Clients	4.2	52.7	115%
(4) Improved Services, 3934 Clients	6.8	59.5	130%

fiscal situation was sufficiently dire, decision packages 1 and 2 would obviously receive the greatest amount of executive and legislative scrutiny. Conversely, if the choice was made to increase funding for this subprogram, packages 3 and 4 would assume major importance.

*“A singularly important strength of ZBB in those states using a PPB system is the fact that it helps to ‘fill the gaps’ of a program structure, and thus complements the budget process already in place. . . . There is no other system of budgeting that requires the decremental/incremental approach in terms of service level, as ZBB does.”*

To carry this approach one step further, Table 8 outlines the basis upon which the Northern Virginia Training Center (NVTC) might develop its supporting data to fall within the subprogram aggregation.

Though the number and percentage costs of the decision packages are identical to those on Table 7, the institutional display for NVTC demonstrates that the five major activities carried out at the institution are affected in significantly different ways

Table 8

NORTHERN VIRGINIA TRAINING CENTER FOR THE  
MENTALLY RETARDED

<u>Decision Packages</u>		<u>FY 1978-79 Cost (Millions)</u>	<u>Percentage FY 1977-78 Expenditures</u>
<u>Minimum Level, 222 Patients</u>			
Administration	(1)	.295	100%
Care & Treatment of Patients	(1)	2.325	92%
Maintenance of Bldgs. & Grounds	(1)	.750	88%
Education and Training	(1)	-0-	-0-
Food Service	(1)	<u>.451</u>	<u>100%</u>
Totals		3.821	90%
<u>Current Level, 222 Patients</u>			
Administration	(2)	.313	106%
Care & Treatment of Patients	(2)	2.686	106%
Maintenance of Bldgs. & Grounds	(2)	.882	103%
Education and Training	(2)	.119	106%
Food Service	(2)	<u>.500</u>	<u>111%</u>
Totals		4.500	106%
<u>Current Level, 285 Patients</u>			
Administration	(3)	.324	110%
Care & Treatment of Patients	(3)	2.950	117%
Maintenance of Bldgs. & Grounds	(3)	.939	110%
Education and Training	(3)	.129	115%
Food Service	(3)	<u>.541</u>	<u>120%</u>
Totals		4.883	115%
<u>Improved Services, 285 Patients</u>			
Administration	(3)	.324	110%
Care & Treatment of Patients	(4)	3.294	130%
Maintenance of Bldgs. & Grounds	(3)	.939	110%
Education and Training	(4)	.422	278%
Food Service	(3)	<u>.541</u>	<u>120%</u>
Totals		5.520	130%



by the availability of resources. In package 1, for instance, it would probably be decided that it would be impossible to cut food service and administrative activities below FY 77-78 levels. Thus, to reduce overall expenditures to a level of 90% of FY 77-78 costs, education and training and building maintenance would bear the brunt of spending reductions.

At the opposite extreme it would be reasonable to assume that education and training, and the general care and treatment of patients, would benefit the most from a significant infusion of additional funding for FY 78-79.

It is my opinion that the development of program budget requests in this ZBB format, for selected areas only, allows detailed executive and legislative budget review in a manner that increases understanding of the basic issues involved. It also lends itself to effective follow-up, since service levels are explicitly identified with alternative funding levels.

May I answer any of your questions at this point?

Question

Suppose you recommended some type of rotating ZBB. Would you have an opinion on who should be the proper person to do it?

Mr. Fogarty

Well, I think that if the General Assembly decides that it wants to go to some form of Sunset, and if the standing committees decide that they are going to review a given policy area every three or four years, the money committees could rotate ZBB to review these areas at the same time. I do not think it is a question of one committee doing it to the exclusion of others. I think it requires working together so that the budget bill will reflect some of the findings of the standing committees.

Question

You have indicated that going to Zero-Base budgeting across the board would be a mistake, and just the same kind of problem, I think, has been indicated to us regarding the adoption of Sunset across the board. So, if the General Assembly were to decide to do something in this area, on a selective basis, did I understand you correctly to say that you think that Sunset and Zero-Base budgeting should be tied in together as a package, but on a sequential basis?

Mr. Fogarty

You do not need to do ZBB to have an impact on a program system; you can go ahead and just make an ad hoc decision and cost it out in the budget process. But if one of the things you are

concerned with is whether a program should be funded at 100% of current spending levels, more, or perhaps less than that, a ZBB format can be very useful. So on a rotating basis I think you could engage in a special activity to do Zero-Base budgeting, in addition to program budgeting.

#### Question

One of the problems we have seen with the implementation of Zero-Base budgeting is the lack of proper motivation and training. It is fairly evident in the New Jersey situation. If this were to operate on an ad hoc basis, how would you envision providing the training and the motivation to those selected agencies to present their budget in the proper format?

#### Mr. Fogarty

I think you would have no problem with motivation in general terms because the scrutiny the General Assembly or the Governor focused on one particular agency, or program, would prompt a strong effort to provide the best information possible.

The other part of the question is more difficult to answer. Can we train budget analysts and management staff in the agencies to put together the format? Can we have program managers deal with these types of questions at different resource levels? I am not as optimistic about that. I think that would be a learning process and perhaps pretty torturous.

#### Question

The presentation that you have just made to this group is a limited adaption of ZBB to a particular program or aspects of a program. If you change the label to "modification of program budget as it exists in Virginia," do we really have a different system? Or are we dealing essentially in semantics? And if we were to make some refinements in the present programming level aspect of our program budget, we have gone through essentially the same process. The same data would be supplied and the same data would be analyzed and hopefully with as good a judgment having been made.

#### Mr. Fogarty

The only qualifier I would add to that would be that this requirement would be over and above the current program requirements. Remember that I mentioned "filling in the gaps". This would require agencies to do more than is now expected of them. It would make them develop levels of resources congruent with levels of services.

Thank you.

# Virginia's New Program Budgeting System

Maurice B. Rowe

We are pleased to present a panel discussion on program budgeting and the Sunset concept in Virginia. As directed by the General Assembly, we have been at work since 1975 to implement provisions of Chapter 27, Title 2.1, of the *Code of Virginia*. Basically, this provides for a program budgeting system that will improve our effectiveness in planning and programming and better serve the decision-making process of the General Assembly.

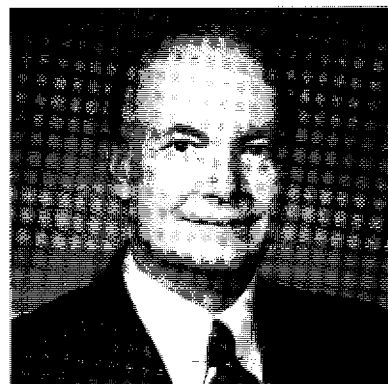
The Commission on State Governmental Management has made a number of recommendations which have been adopted by the legislature, one of which is the program budgeting system. As we look at the work and recommendations of the commission, I believe we will find that major focus has been placed on improving our organizational structure of State government and the thrust has been on developing accountability processes for both the legislative and executive branches.

## New Information Systems

In preparation for the program budgeting system, several major management information systems have been designed and are either partially on-stream or will be by July 1, 1978. The Personnel Management Information System will automate personnel transactions, both the preemployment requirements and actions for personnel administration. The accounting information system is partially on-stream and providing information on budgeted funds and expenditure actions. It also provides current data on total expenditures for the several types of funds and revenue collections. A more expanded accounting system phase will come on-stream on July 1, 1978. In addition, we are developing a budgeting information system, a part of which has been in use for about one year.

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Maurice B. Rowe is the Secretary of Administration and Finance. Mr. Rowe has a long history of State service and holds the distinction of being the first career employee to be promoted to a Secretarial position. Mr. Rowe is a past president of the Virginia Academy of Science. He is a graduate of the Virginia Polytechnic Institute and State University.



Other components will be coming on-stream in the near future with the final system to commence on July 1, 1978, but with full recognition that refining will be necessary as we proceed with the future budget cycles. With these systems, we will bring into focus a financial management system for State government. We are now identifying the requirements of the legislative and executive branches to develop the financial management system from components of the other systems which have been mentioned in order to provide certain types of data for policy and management decisions.

#### Information to Support Legislative Oversight

We fully recognize and encourage a commitment by the legislature to provide oversight of executive programs. A great deal of this is ongoing and continues by committees, as well as by individual members of the legislature. A more formalized approach might have value and we encourage a systematic overview or evaluation of executive performance. To facilitate this thrust, we are interested in developing our systems to furnish the type of information which will be needed in the evaluation process.

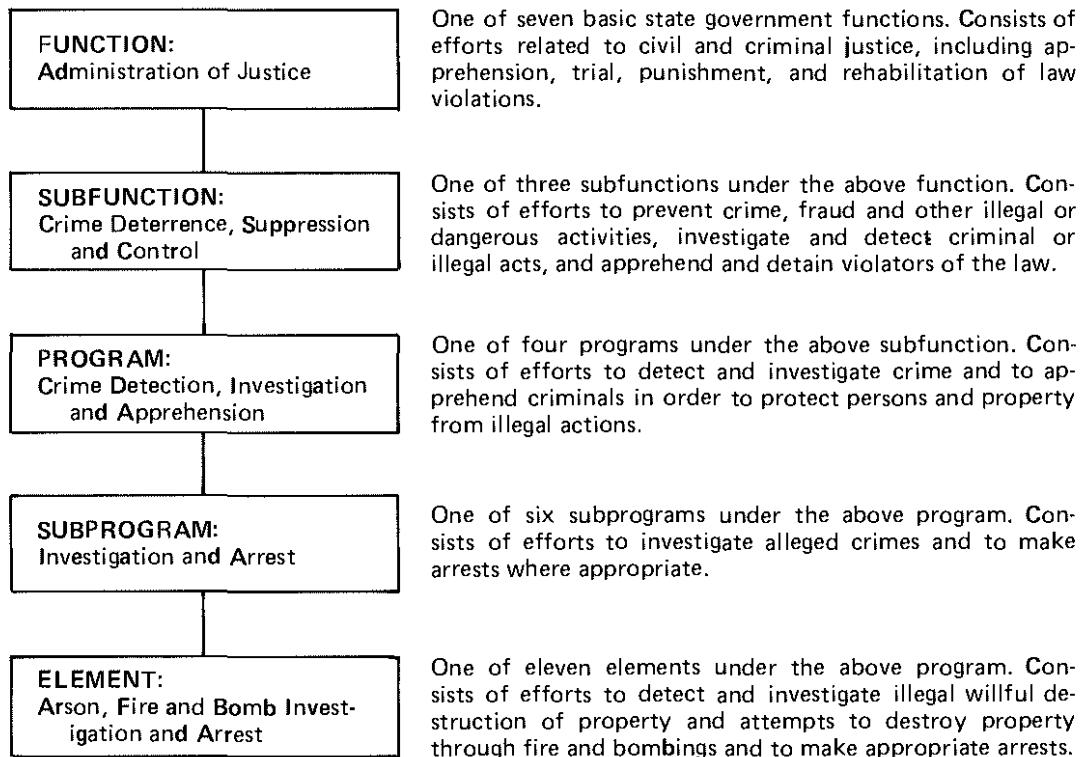
*“We fully recognize and encourage a commitment by the legislature to provide oversight of executive programs. . . . A more formalized approach might have value, and we encourage a systematic overview or evaluation of executive performance. To facilitate this thrust, we are interested in developing our systems to furnish the type of information which will be needed in the evaluation process.”*

In the development of the program budgeting system, we have undergone some trials and tribulations, particularly in laying upon our agencies and institutions considerable new work load. This has occurred in addition to those requirements which have arisen as a result of expenditure reductions and the numerous other executive actions taken to improve our total management or monitoring of State government operations. We hope these types of requirements will be minimized as we automate the several management systems. I believe the program budgeting system will put in place a great deal of data that may be called upon without having to resort to manual input from agencies and institutions in future budget cycles.

### Building Blocks of the Program Structure

The program structure has been designed to support program budgeting requirements established by the General Assembly. The system addresses numerous purposes. Among them it seeks to improve planning, budgeting, program operations, financial control, analysis and organizational structuring. The program structure enhances the ability of decision-makers and program managers to compare objectives with results and to aggregate costs by each unit across departmental lines. All state agency programs and their component parts are classified in the document "Virginia State Government Program Structure."

There are five levels of this structure: functions, subfunctions, programs, subprograms and elements. The functional level is the broadest subdivision and it expresses the general purpose of an entire area of government. There are seven functional program areas: 1) Administration of Justice, 2) Education, 3) Individual and Family Services, 4) Resource and Economic Development, 5) Transportation, 6) General Government and 7) Enterprises. The following illustration shows how a particular element is related to the function of which it is a part.



Existing legislative requirements for the biennial budget contain two principal characteristics; control budgeting and program budgeting. Control oriented budgeting requirements focus on the costs of inputs (e.g., personnel services, contractual services, equipment) necessary to operate a program. Program oriented budgeting focuses on the outputs (services provided) of the program operation.

All requirements of the biennial budget legislation are being addressed; however, as alluded to above, some of the new provisions are being considered developmental or in a test environment. With this in mind, the requirements both preexisting and new are identified below as either control or program budget provisions.

1. Preexisting Control Budget Provisions

- a. Budget document, organized by function, primary agency, and program showing in separate parallel columns;
  - (1) amount appropriated for the last preceding appropriation year;
  - (2) amount expended in the last preceding appropriation year;
  - (3) amount appropriated for the current appropriation year;
  - (4) agency's request for each year of the ensuing biennium;
  - (5) Governor's recommendation for each year of the ensuing biennium.
- b. Data shall be included for major objects or classes of expenditure data at the appropriation level using columnar headings specified in (a.) above.
- c. A statement of revenues and expenditures for each of the two years next preceding, by budget classifications.
- d. A statement of debts and funds.
- e. A statement of itemized estimates of State treasury as of the beginning and end of each of the next two appropriation years.
- f. An itemized financial balance sheet at the close of the last preceding fiscal year ending June 30.
- g. A general survey of the State's financial and natural resources, with a review of the general economic, industrial, and commercial condition of the State.
- h. Statements showing:
  - (1) estimated additional annual costs of maintenance and use of each item of capital outlay;
  - (2) estimated additional costs of each new service recommended in the plan of proposed expenditures; and
  - (3) estimated number of additional personnel and their salaries and other costs.

### How the Program Structure is Reflected in the Budget Bill

Shown below is an example of a model page from the 1978-80 Budget Bill that will be presented to the General Assembly.

The Rehabilitative School Authority is a State agency charged with the responsibility for all educational programs within institutions operated by the Department of Corrections.

The activities of the agency have been categorized into two major program areas: Administrative and Support Services (Item ba.) and Instruction (Item bb.). The instruction program is further divided into two subprograms.

Dollar amounts listed in the two columns on the left (Information References) are details of sub-program costs and fund sources. The total of the fund sources must add to the amounts appropriated, which are shown in the two columns on the right. The total (by year) for the agency is also provided.

		Information References (\$)		Appropriations (\$)	
		First Year	Second Year	First Year	Second Year
<b>\$ 33. REHABILITATIVE SCHOOL AUTHORITY (750)</b>					
Item ba.	Administrative & Support Services (1990000) . . . . . (General Management & Direction 1990100)			\$00,000	\$00,000
	Out of this appropriation shall be paid:				
	the salary of the Director,				
	\$00,000 the first year, \$00,000 the second year.				
	Fund Sources: General . . . . .	\$0,000	\$0,000		
	Federal Trust . . . . .	\$0,000	\$0,000		
	Special . . . . .	\$0,000	\$0,000		
Item bb.	Instruction (1970000) . . . . .			\$00,000	\$00,000
	Subprograms: Basic Skills & Knowledge Instruction				
	(1970100) . . . . .	\$0,000	\$0,000		
	Occupational-Vocational Education				
	(1970300) . . . . .	\$0,000	\$0,000		
	Fund Sources: General . . . . .	\$0,000	\$0,000		
	Federal Trust . . . . .	\$0,000	\$0,000		
	Special . . . . .	\$0,000	\$0,000		
	Total for Rehabilitative School Authority . . . . .			\$00,000	\$00,000
	Fund Sources: General . . . . .	\$0,000	\$0,000		
	Federal Trust . . . . .	\$0,000	\$0,000		
	Special . . . . .	\$0,000	\$0,000		

- i. A complete and itemized plan of all proposed expenditures for the State and estimated revenues and borrowings for each year.

#### 2. New Control Budget Provisions

- a. Summary data of positions authorized and funded, or proposed for authorization and funding, shall be shown at the appropriation and program levels, by type of fund, using the columnar hearings specified in (1. a.) above.
- b. Increases in expenditure recommended in the biennium shall be distributed at the program level by:
  - (1) costs to continue the present level of activities;

- (2) costs to process increases in work load;  
and
  - (3) costs related to new or changed services.
- c. As nearly as practicable, the distribution of the total budget should be by program, indicating authority:
  - (1) mandated by federal government;
  - (2) necessary to avoid losses in federal revenue;
  - (3) mandated by Virginia statute; and
  - (4) discretionary.

### 3. New Program Budget Provisions

- a. Budget analysis providing narrative justifications including goals, objectives, strategies, and program measures as well as recommendations at the functional and program levels.
- b. Governor's Program Statement presenting the Governor's goals, objectives, and policies.
- c. Six-year revenue plan providing general fund and non-general fund revenue projections for the 1978-84 period.
- d. Six-year expenditure plan providing general fund and non-general fund expenditure projections for the 1978-84 period.
- e. Determination of work load indices and other indices and other criteria to be used in both budget evaluation and post audit evaluation.
- f. Proposed appropriations shall be structured to incorporate all closely related programs of an agency within a single appropriation; identity of major programs and related costs shall be retained as discrete parts of each appropriation item for information purposes.

There is no doubt that we are involved in a learning process. We are learning to develop a program structure and to plan and develop the budget on a program basis. I believe the members of the General Assembly will also be in a learning process for the 1978-80 budget as they first approach this budget with a program identification and allocation of funds rather than a traditional agency specific activity basis. You will have the opportunity to note the costs of programs; in other words, what we are funding to crime deterrence, suppression and control programs; what it is costing for the administration of justice function.



In looking at the Sunset evaluation process, a great deal of information will be available as a result of identifying functions and programs in the budget process. We will have the opportunity to evaluate the goals and objectives for each of the programs along with the strategies for achieving these goals and objectives.

In addition, and of great importance, is how we measure the results of performance. As the legislature reviews the budget, there will at least be the opportunity to judge the value of goals and objectives of the programs. In carrying this forward, you may decide what additional information is necessary as you proceed to expand the evaluation process beyond that of the budget, and include other factors for prioritizing and establishing values.

HOUSE JOINT RESOLUTION NO. 178

*Instructing the Joint Legislative Audit and Review Commission to conduct a study of "Sunset" legislation.*

Patrons—Lane, Gunn, Manning, Slayton, White, Pickett, Bagley, R.M., Ball, Dickinson, Cranwell, Scott, Diamonstein, Robinson, Jones, G.W., Sanford, Heilig, Glasscock, Callahan, Teel, Brickley, Fickett, Harris, Geisler, Campbell, McClanan, Creekmore, Parker W.T., McMurtrie, Pendleton, Marshall, Baliles, Allen, Melnick, Rothrock, Thomson, Council, Guest, James, Sisisky, Sheppard, McMurran, Vickery, Morrison, Grayson, and Thomas

Referred to the Committee on Appropriations

WHEREAS, the government of the Commonwealth of Virginia has become exceedingly complex and its cost has outstripped available resources; and

WHEREAS, agencies and programs need to be periodically monitored and evaluated by the General Assembly using the most modern procedures and techniques available; and

WHEREAS, public problems already addressed may change, necessitating periodic reevaluation of legislative programs; and

WHEREAS, the Commonwealth has already taken several steps toward achieving a higher degree of accountability, efficiency and economy in the government including:

- (i) a reorganized executive branch,
- (ii) a program budget structure and presentation for the General Assembly,
- (iii) a strengthened management process, and
- (iv) a competent legislative oversight capability; and,

WHEREAS, the concepts of (1) legislation which requires the General Assembly to reaffirm continuation of programs or agencies after a specified time period, commonly known as "Sunset"; (2) comprehensive legislative program evaluation; and, (3) Zero-Base or other comprehensive forms of budget analysis deserve study and consideration as possible ways to create and coordinate the best aspects of legislative and executive responsibility to achieve more responsive, economic, and effective public programs; and

WHEREAS, making the best use of these new techniques in State government requires careful study of procedures and attendant problems in advance of enactment; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Joint Legislative Audit and Review Commission be instructed to undertake a study of the "Sunset" concept and prepare a report to the Governor and the General Assembly at the nineteen hundred seventy-eight Session of the General Assembly. If deemed appropriate, the report should present draft legislation and a plan for legislative implementation which specifies alternative procedures, costs, and potential benefits to the Commonwealth.

The commission shall ensure full participation by all interested members of the General Assembly, executive officials, and the public through hearing and conferences. The Joint Legislative Audit and Review Commission shall be assisted by a twelve-member advisory task-force appointed in the following manner: (i) two members appointed by the Governor of which one appointee shall not hold elective office; (ii) six members appointed by the Speaker of the House of Delegates of which one appointee shall not hold elective office; (iii) four members appointed by the Senate Committee on Privileges and Elections of which one member shall not hold elective office. The report of the commission shall be approved by a majority of the combined membership of the Joint Legislative Audit and Review Commission and the twelve-member task-force appointed herein.

The study shall include but not be limited to: (1) the scope of coverage of "Sunset" legislation, required exemptions, and the timeliness and categories of program review; (2) criteria that should be used to evaluate agencies or programs; (3) the role of and relationship between standing committees, other legislative commissions and service agencies, and the executive; (4) the mechanics of implementation and operation; and (5) the costs involved.

The expenses incurred in the course of this study, including any per diem and travel allowances of task-force members, shall be paid from the appropriation to the Joint Legislative Audit and Review Commission.

823 EAST MAIN STREET—RICHMOND, VIRGINIA 23219—(804) 786-1258

